



Insolvency in Portugal

A brief explanation of the proceedings
and statistical overview

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A - A brief explanation of the proceedings of Insolvency in Portugal

1. Aims of the non-judicial and judicial insolvency proceedings in Portugal

Under Portuguese law, “insolvency” is defined as a debtor’s inability to meet his commitments as they fall due.

Legal persons, and autonomous groups of assets and liabilities where no individual has unlimited personal liability for the debts, are also considered to be insolvent when their liabilities clearly exceed their assets.

Potential insolvency becomes actual insolvency in cases where the debtor applies to or the creditors ask the court for a declaration of insolvency.

The law offers an extra-judicial conciliation process to permit the rehabilitation of companies facing insolvency or experiencing financial difficulties. This process is conducted by a public entity, the Institute for Support to Small- and Medium-sized Enterprises and Investment (IAPMEI).

The aim of this procedure is to reach an agreement between the company and all or some of its creditors that will pave the way for a viable recovery.

The fact that judicial insolvency proceedings are pending is no bar to the extra-judicial conciliation process. In that case, if insolvency has not yet been declared, the legal process can be suspended at the request of the debtor or of any interested party.

The agreement reached in the conciliation procedure must be set out in writing, and a public deed is legally required in certain cases.

¹ Source: http://ec.europa.eu/civiljustice/bankruptcy/bankruptcy_por_en.htm

The Insolvency and Corporate Recovery Code ([Código da Insolvência e da Recuperação de Empresas](#)) provides for a single type of judicial proceedings without distinction between corporate recovery and insolvency.

Creditors are required to assess the company's financial viability and decide jointly whether recovery or liquidation is appropriate, and in what terms.

The law also provides for a further process to liquidate the debtor's assets and grants creditors the option to approve a plan which does not involve liquidation.

For the Insolvency proceeding that concerns a physical person and not a legal one there's the possibility for the judge to establish a 5 year payment plan at the end of which all unpaid debts are considered unrecoverable and the debtor has a fresh start.

2. Conditions for opening an insolvency proceeding

To initiate these proceedings, it has to be shown that the debtor is unable to meet liabilities as they fall due or, where legal persons and autonomous groups of assets are concerned, that the liabilities are clearly higher than the assets.

Insolvency proceedings can be initiated when any of the following events occurs:

- General suspension of payment of debts due for settlement;
- Failure to comply with one or more obligations which, by virtue of their size or of the circumstances of the failure, show that the debtor is generally unable to meet his obligations as they fall due;
- The disappearance of the company's owner or of the debtor's directors, or the act of abandoning the head office or main centre of activity as a result of the debtor's insolvency, and without the designation of a suitable replacement;
- The dissipation, abandonment, hasty or grossly uneconomic liquidation of assets and the creation of fictitious claims;
- The lack of adequate assets to secure payment of the claimant's debt as adjudged in enforcement proceedings brought against the debtor;
- Failure to comply with obligations contained in an insolvency or repayment plan approved by creditors in insolvency proceedings already under way;

- General failure, in the previous six months, to meet debts in respect of tax and social security payment and contributions, debts arising from an employment contract or from the breach or termination of such a contract, rentals for any type of hire, including financial leases, installments of the purchase price or loan repayments secured by a mortgage on the debtor's business premises, head office or residence;
- A clear excess of liabilities over assets in the latest approved balance sheet, or a delay of more than nine months in approving and filing accounts, where a legal obligation to do so exists, where the debtor is a legal person or autonomous group of assets and liabilities.

3. Role of the various participants in each type of proceedings

a. The court

The judicial insolvency procedure must be initiated in the court of the debtor's head office or domicile or, in the case of the insolvency of an unclaimed deceased estate, at the court of the deceased's domicile at the time of death.

Application for a declaration of insolvency may also be made to the court in the location of the debtor's principal interests – this being defined as the place where he normally administers his affairs and which is recognizable as such by third parties.

The court assumes the key role of ensuring compliance with the legal rules governing the insolvency proceedings, with particular responsibility for making an initial evaluation of the insolvency petition and an assessment of whether the insolvency and payment plans approved by creditors are legal and can be ratified.

It is also required to assess a debtor's alleged insolvency in the light of the facts emerging during the proceedings and, if it considers that the facts justify it, to issue a declaration of insolvency – although without the need to give an opinion on the company's potential for recovery.

The judge is responsible for ruling on the proof of debts and their ranking, and may also appoint a trustee for persons lacking legal capacity, and order suspension of the liquidation of the assets and the distribution of proceeds among the creditors.

Similarly, it is the court which orders closure of the proceedings.

b. The administrator

The administrator is appointed by the judge who, when making the appointment, is required to take note of suggestions made by the debtor or by the creditors' committee, where one has been formed. However, a creditors' meeting may vote to replace the administrator appointed.

The administrator's responsibilities, with the cooperation of, and subject to examination by the creditors' committee, are as follows:

- To prepare for payment of the insolvent party's debts from the cash available in the estate (the debtor's assets), namely the proceeds of the asset sales he is required to promote;
- Over the longer term, to protect the insolvent person's rights and allow him to continue exercising them, and to enable the company to continue operations, if applicable, avoiding as far as possible any deterioration in its financial situation.

c. The creditors' committee

This is an optional body, whose existence and makeup are dependent on the wishes of the creditors' meeting. The meeting may dispense with the committee nominated by the judge or may appoint one if he has failed to do so, and, in either case, may alter its makeup.

The court may refrain from appointing a committee where it considers this is justified in view of the limited size of the assets, the straightforward nature of the liquidation or the small number of creditors.

Where a committee exists, its agreement is required for legal acts of particular significance for the procedure.

d. The debtor

The debtor is required to apply for a declaration of insolvency within sixty days from the date on which he becomes aware of his insolvency, or on the date by which he should have become aware of it, except in the case of an individual who, on the date when insolvency occurs, is not the owner of a company.

If the debtor is the owner of a company, there is a legal presumption of awareness of the situation of insolvency three months after a general failure to meet its tax or social security obligations or its obligations arising under employment or rental contracts.

During the proceedings, the insolvent debtor is required:

- To supply all relevant information requested by the administrator, creditors' meeting, creditors' committee or by the court;
- To attend the court personally where so required by the judge or administrator, unless legitimately prevented from attending or where he has been expressly allowed to be represented by an agent;
- To provide all cooperation as requested by the administrator to enable him to carry out his role.

e. The creditor

The creditor is the leading figure in the insolvency process.

He is entitled to request that the debtor be declared insolvent, and may also withdraw the application or abandon the proceedings, until such time as the final decision is made. If the court rejects the insolvency petition, he may (provided he is the petitioner) appeal against the decision.

He may participate in the creditors' meeting at which he has the power to decide, with absolute discretion in terms of the future of the company, whether it should be rehabilitated or liquidated, and in what terms.

He may accept or reject the payment program where the debtor submits one.

He has the right to have the court-appointed administrator replaced, and may exercise the above-mentioned powers through the creditors' meeting.

Right of appeal is limited to one level – i.e. appeal is only possible to the Court of Appeal. The only exception to this is in situations involving appeals against judgments in areas for which there is currently no uniform jurisprudence.

4. Effects of opening of proceedings

a. Definition of the estate

Unless stipulated otherwise, the estate of an insolvent party comprises all the debtor's assets on the date of declaration of insolvency by the court, together with assets and rights acquired by the debtor while proceedings are pending.

Non-attachable assets only form part of the estate if the debtor proffers them voluntarily and if their non-attachable quality is not absolute.

The law draws a distinction between the insolvency debts and the debts of the estate.

The former are claims on the insolvent party which arose prior to the declaration of insolvency. Claims which the creditor can prove to have arisen during the procedure are treated in the same way.

Debts of the estate are those created during the process, and include, for example, costs of the proceedings and the administrator's remuneration.

b. Effects on the debtor's assets

As regards the debtor's assets, the effect of the declaration of insolvency is to deprive the debtor immediately – either directly or through his directors – of the power to administer and dispose of the assets making up the estate.

With effect from that moment, those powers are vested in the administrator, who takes over the role of debtor's representative for all matters of a financial nature relating to the insolvency.

As a rule, acts undertaken by the insolvent party in breach of these arrangements are ineffectual.

The declaration of insolvency causes all the obligations of the insolvent party which are not subject to a condition precedent to become due for settlement.

c. Claims

Four categories of claim exist in the insolvency proceedings: secured, preferential, subordinated and unsecured.

Secured claims are those with security *in rem* over assets in the estate, up to the value of such assets. They also include special creditors' preferential claims. This category not only covers the claims but also the interest on them.

Preferential debts are general creditors' preferential claims over assets in the estate, up to the value of the assets over which such preferential claims exist, and where the claims are not extinguished as a consequence of the declaration of insolvency

Subordinated claims are those which will be settled only when the unsecured creditors have been paid in full.

The following claims are subordinated, except where they carry general or special creditors' preferential rights, or are secured by legal mortgages which are not extinguished as a result of the declaration of insolvency:

- The claims of persons with a special relationship with the debtor – such as the spouse, ascendants, descendants or siblings of the debtor (where a physical person is involved) or the shareholders, partners or persons who have been in a controlling or group relationship with the debtor, where it is a legal person – and of those to whom such claims have been transferred in the two years prior to the start of insolvency proceedings;
- Interest on non-subordinated claims arising after the declaration of insolvency, except for those covered by security *in rem* and by general creditors' preferential rights up to the value of the assets in question;
- Claims which are subordinated by agreement between the parties;
- Claims relating to services provided free of payment by the debtor;
- Claims against the estate which, as a result of decisions benefiting the estate itself, are held by a third party not acting in good faith;
- Interest on subordinated claims arising after the declaration of insolvency;
- Claims in respect of shareholders' loans.

Unsecured claims are all those not covered by the above categories.

d. Interim measures

Where there are justified fears of maladministration, the judge, on his own initiative or at the petitioner's request, may order the protective measures necessary or appropriate to prevent any worsening of the debtor's financial situation until such time as the declaration is made.

These measures may include, for instance, the appointment of a temporary judicial administrator with exclusive powers to administer the debtor's assets, or to assist the debtor in administering them.

5. Specific rules relating to certain categories of claims

With the declaration of insolvency, the following claims are extinguished:

- General creditors' preferential rights attached to claims against the estate held by the State, local authorities and social security institutions, and which arose more than twelve months prior to the onset of insolvency proceedings;
- Special creditors' preferential rights attached to claims against the estate and held by the State, local authorities and social security institutions, and which were due and payable more than twelve months prior to the onset of insolvency proceedings;
- Legal mortgages for which an application for registration was made in the two months before the date of the onset of insolvency proceedings and which secure claims against the estate, where the mortgagee is the State, local authorities or social security institutions;
- If dependent on registration, security *in rem* over registrable real or movable property forming part of the estate, supporting claims against the estate and already in existence but not yet registered or where registration has not yet been applied for;
- Security *in rem* over assets forming part of the estate and securing claims judged to be subordinated.

6. Rules relating to detrimental acts

The law stipulates that, as a general rule, all acts within four years prior to the onset of insolvency proceedings may be avoided if they diminish, frustrate, hinder, threaten or delay the settlement of creditors' claims.

As a rule, avoidance presupposes bad faith by the third party, which is presumed in the case of acts undertaken or omitted within two years prior to the onset of insolvency proceedings and involving a person in a special relationship with the insolvent party, or

from which such a person benefited, even if the special relationship did not exist at the time in question.

Once acts prejudicial to the estate have been avoided – with retroactive effect – the situation which would have existed if the action or omission had not occurred has to be reinstated.

7. Conditions for the lodgment and admission of claims

In the insolvency declaration a period of up to thirty days is set during which creditors must apply for their claims to be admitted. As far as known creditors are concerned, this period begins from the date of service or notification of the creditor. For other creditors, the deadline is extended by five days and the period starts on the date of publication of the last notice in the Portuguese Official Gazette, or in a wide-circulation national newspaper (and now, also, online - <http://www.citius.mj.pt/Portal/consultas/ConsultasCire.aspx>).

8. Rules relating to reorganization proceedings

Under Portuguese rules, creditors have to decide whether payment of their claims will be achieved by a full liquidation of the debtor's assets, or by restructuring the company and keeping it in business, either under the ownership of the debtor or of third parties. Their views must be set out in an insolvency plan approved in the creditors' meeting. If they opt for recovery, the creditors are at liberty to choose the most appropriate measures to achieve it.

9. Rules relating to the winding-up proceedings

In the creditors' meeting called to assess the administrator's report produced following the declaration of insolvency, a decision is also taken on whether the debtor's establishment or establishments forming part of the assets of the estate must be kept going or closed down.

However, where authorized by the creditors' committee, or where not so authorized but where the debtor does not object, or where the debtor objects but the judge authorizes it, the administrator may close down the debtor's establishments prior to the date of the meeting called to assess the report.

If the creditors' meeting instructs the administrator to prepare an insolvency plan, it may order suspension of the liquidation and distribution of the assets. This suspension ceases if the plan is not submitted within the following sixty days or if it is not approved.

10. Conditions for the closure of the proceedings

Insolvency proceedings may be closed immediately with the declaration of insolvency where there are indications that the company's assets are insufficient to pay the costs of the proceedings and the expected debts of the insolvent estate.

Normally they're closed when:

- All debts have been paid;
- When there's no more assets that can be sold to pay the remaining debts.

11. Consequences for the debtor or for the administrators that are found to have caused the insolvency with intent

When the judge rules that the insolvency was caused with intent he condemns the debtor or its administrator to:

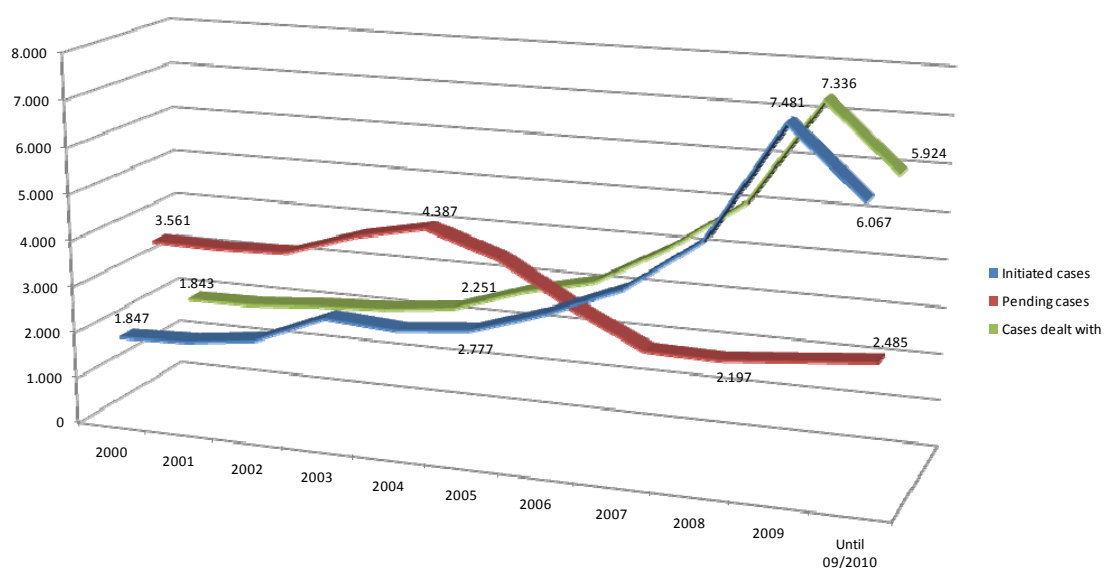
- To be deprived of the power to administer and dispose of his assets, by a period of 2 up to 10 years, and having an administrator assigned;
- Being unable to have a business or being limited in his rights concerning taking part in any administrative body of any legal person with an economical goal, by a period of 2 up to 10 years; and
- Lose his credits over the estate or the insolvency.

The sentence is registered in the civil and commercial registry.

B – A statistical overview of Insolvency in Portugal

Referring to the statistical overview of the last decade, the insolvency proceedings registered the following evolution:

Chart 1
Evolution of Insolvency Proceedings from 2000 to 2010²



Source: DGPJ (official source)

There are three important facts concerning this evolution:

- First, the number depicted for the year 2010 relate only to the first 9 months, and, if the rate is maintained in the following months, every indicator will have numbers larger than reported in the year 2009;
- Second, although the number of initiated cases register an increase over the first 6 years, the rate of increase is over three times greater (50% from 2000 to 2005; 169% from 2005 to 2009);
- Third, and more importantly, since 2004 (when the new legislation became applicable) the number of pending cases (that were increasing at an average of 6% a year, from 2000 to 2004) decreased 50% in 4 years (from 4.387 in 2004

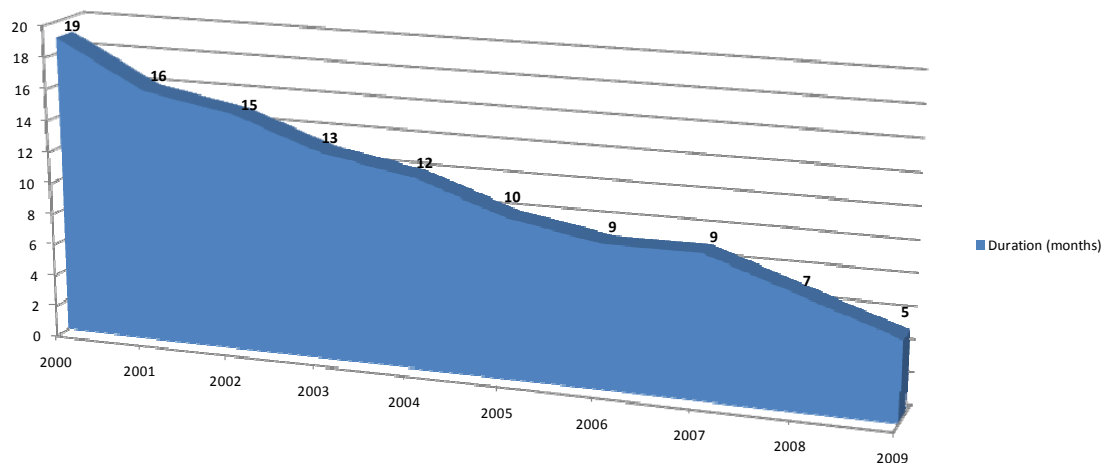
² Since 2007 the data started to be collected automatically through an interface with the case management software installed in all first instance courts.

The data relating to 2010 are not yet validated and have a merely indicative nature. They should not be treated with the same reliability as the data concerning other years.

to 2.197 in 2008) and in the last 2 years (2008 to 2009) the rate of increase of cases pending is much lesser (7%) than the rate of increase of initiated cases (49%).

As to the duration/length of the proceedings the following chart demonstrates the evolution occurred in the last decade.

Chart 2
Duration of Insolvency Proceedings from 2000 to 2009
(Average duration in months)



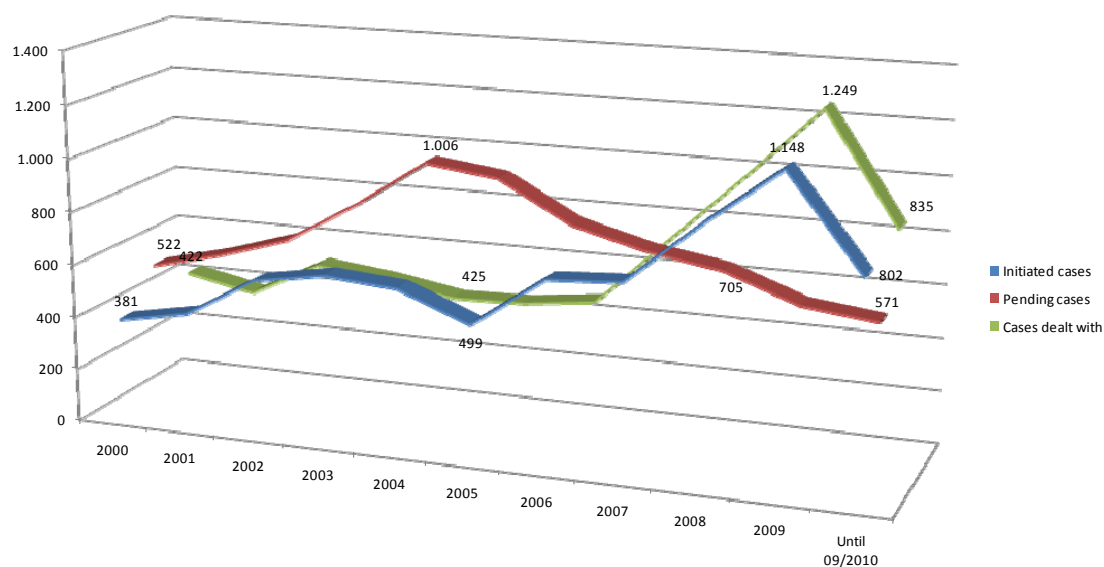
Source: DGPJ (official source)

As it results clear from the analysis of the chart, the average duration of insolvency proceedings was reduced to a quarter of the duration that it had only 10 years ago, in spite of the fact that the initiated proceedings increased over 3 times in that period (from 1.847 in 2000 to 7.481 in 2009).

The insolvency cases are dealt with in unspecialized courts throughout the country but, in the metropolitan areas of Lisbon and Oporto there are specialized courts dealing with insolvency cases.

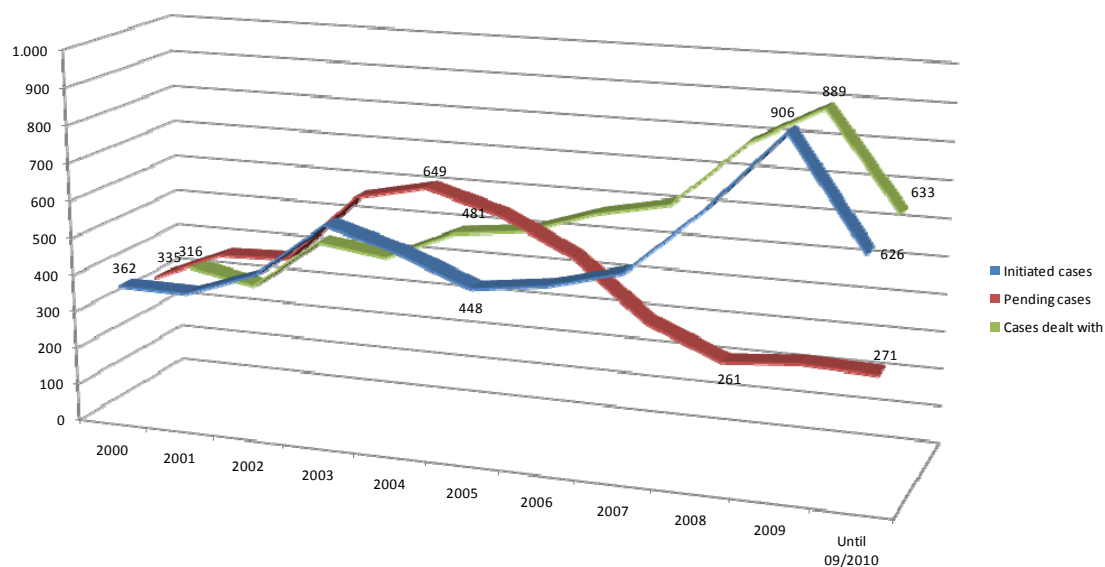
Concerning the evolution of insolvency proceedings, in the last decade, the specialized courts do not differ as much from the general overview of the country.

Chart 3
Evolution of Insolvency Proceedings from 2000 to 2010 in specialized courts³
Lisbon



Gaia (Oporto)

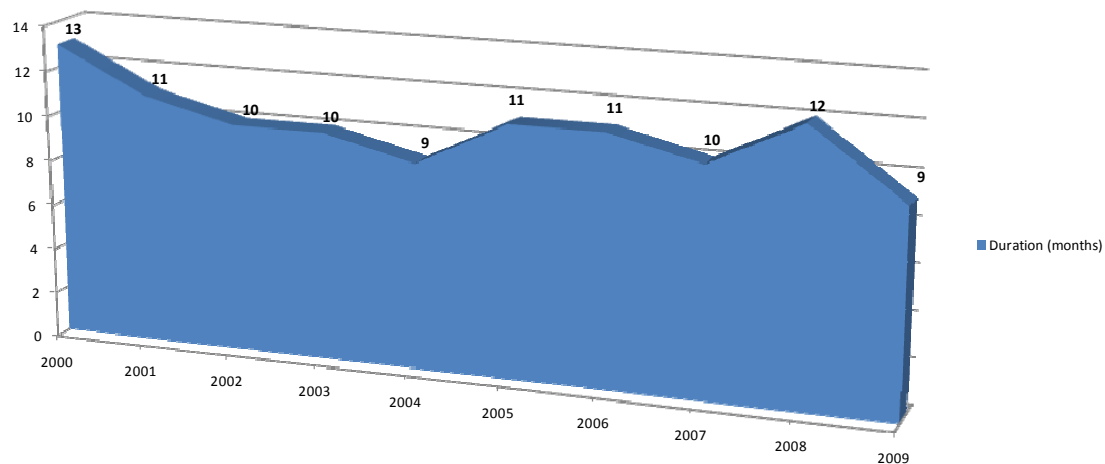
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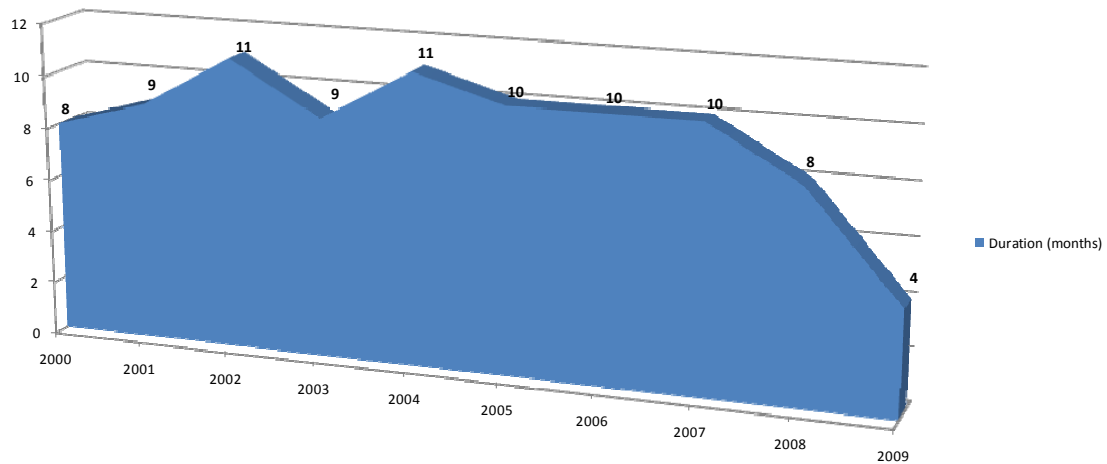
Source: DGPJ (official source)

Concerning the duration of the proceedings there is a clear difference between the evolution and the average duration of proceedings in the specialized courts (specially the commercial court of Lisbon) and the national average. The length of the proceedings in 2009 in Lisbon was almost double the national average.

Chart 4
Duration of Insolvency Proceedings from 2000 to 2009
(Average duration in months)
Lisbon



Gaia (Oporto)



Source: DGPJ (official source)

One final word concerning the difference between the statistical data, shown here, and the courts workload.

The statistical data concerning cases dealt with refers to the declaration of insolvency by the court, and nowadays (since 2004) that declaration is made early on.

When the judicial decision is made that is what matters in terms of considering the case statistically over (and that was the criteria both before and after 2004).

However, although the decision of the judge is now made very rapidly (after 2004) reducing the time that all parties had to wait until a final decision was made, the case does not end there and continues with all of the procedures that lead to the payment of debts. Those procedures are done primarily by the administrator, but some are made still by the judge, and that usually takes several months.

No validated statistical data is collected after the decision of insolvency.